Pinky Rani
Assistant Professor (Guest Faculty)
Department of Economics
Maharaja College
Veer Kunwar Singh University, Ara
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Topic: Business cycle

Business cycles are a type of fluctuation found in the aggregate economic activity of a nation. A cycle consists of expansions in many economic activities occurring at about the same time followed by similarly general contractions. This sequence of changes is recurrent but not periodic.

The business cycle is also referred to as the economic cycle.

- Business cycles are composed of concerted cyclical upswings and downswings in the broad measures of economic activity: output, employment, income, and sales.
- The alternating phases of the business cycle are expansions and contractions.
- Contractions often lead to recessions but the entire phase isn't always a recession.
- Recessions often start at the peak of the business cycle when an expansion ends and end at the trough of the business cycle when the next expansion begins.
- The severity of a recession is measured by the three Ds: depth, diffusion, and duration.

Business Cycle Definition

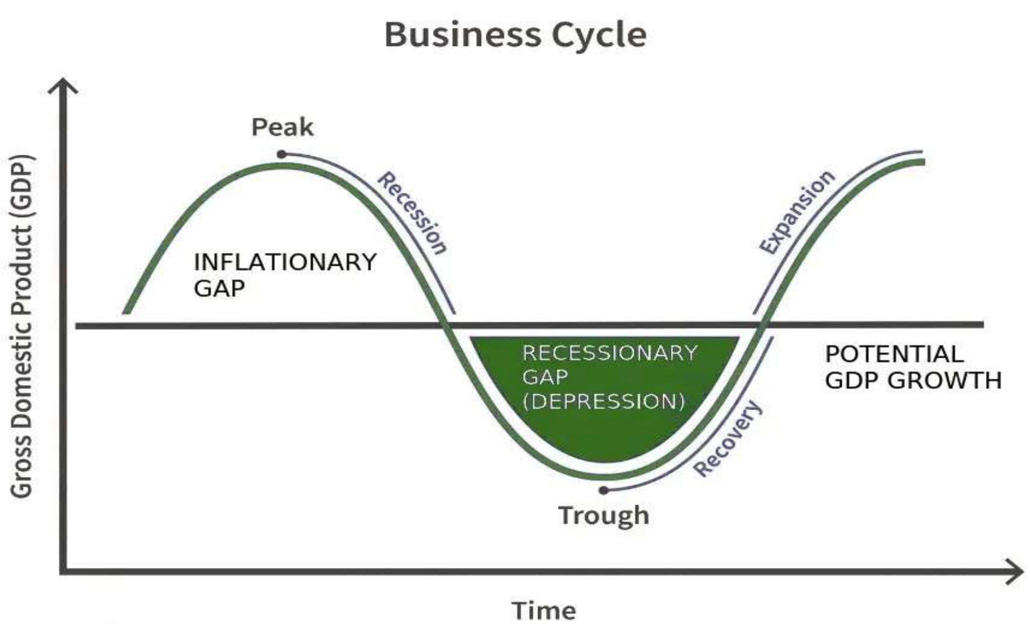
Arthur F. Burns and Wesley C. Mitchel defined business cycle definition as

Business cycle are a type of fluctuation found in the aggregate economic activity of nations that organize their work mainly in business enterprises: a cycle consists of expansions occurring at about the same time in many economic activities, followed by similarly general recessions, contractions, and revivals which merge into the expansion phase of the next cycle; in duration, business cycle vary from more than one year to ten or twelve years; they are not divisible into shorter cycle of similar characteristics with amplitudes approximating their own.

Phases of Business Cycle

Phases of Business Cycle *are:*

1. ***Expansion***
2. ***Peak***
3. ***Contraction***
4. ***Trough***



Let us discuss 4 phases of business cycle in detail:

Expansion

Expansion is the first phase of a business cycle. It is often referred to as the **growth phase**.

In the expansion phase, there is an increase in various economic factors, such as production, employment, output, wages, profits, demand and supply of products, and sales. During this phase, the focus of organisations remains on increasing the demand for their products/services in the market.

The expansion phase is characterised by:

- Increase in demand

- Growth in income
- Rise in competition
- Rise in advertising
- Creation of new policies
- Development of brand loyalty

In this phase, debtors are generally in a good financial condition to repay their debts; therefore, creditors lend money at higher interest rates. This leads to an increase in the flow of money.

In the expansion phase, due to increase in investment opportunities, idle funds of organisations or individuals are utilised for various investment purposes. The expansion phase continues till economic conditions are favourable.

Peak

Peak is the next phase after expansion. In this phase, a business reaches at the highest level and the profits are stable. Moreover, organisations make plans for further expansion.

Peak phase is marked by the following features:

- High demand and supply
- High revenue and market share
- Reduced advertising
- Strong brand image

In the peak phase, the economic factors, such as production, profit, sales, and employment, are higher but do not increase further.

Contraction

An organisation after being at the peak for a period of time begins to decline and enters the phase of contraction. This phase is also known as a **recession**.

An organisation can be in this phase due to various reasons, such as a change in government policies, rise in the level of competition, unfavourable economic conditions, and labour problems. Due to these problems, the organisation begins to experience a loss of market share.

The important features of the contraction phase are:

- Reduced demand
- Loss in sales and revenue
- Reduced market share
- Increased competition

Trough

In Trough phase, an organisation suffers heavy losses and falls at the lowest point. At this stage, both profits and demand reduce. The organisation also loses its competitive position.

The main features of this phase are:

- Lowest income
- Loss of customers
- Adoption of measures for cost-cutting and reduction
- Heavy fall in market share

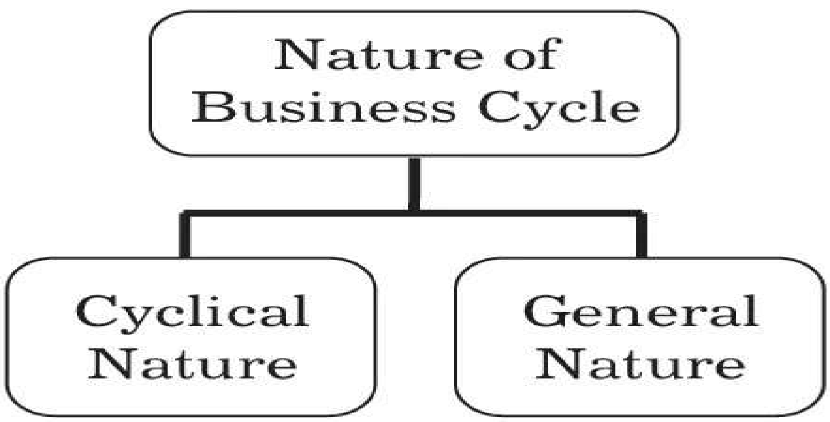
In this phase, the growth rate of an economy becomes negative. In addition, in trough phase, there is a rapid decline in national income and expenditure.

After studying the business cycle, it is important to study the nature of business cycle.

Nature of Business Cycle

The **nature of business cycle** helps the organisation to be prepared for facing uncertainties of the business environment.

1. Cyclical nature
2. General nature



Let us discuss the nature of business cycle in detail.

Cyclical nature

This is the periodic nature of a business cycle. Periodicity signifies the occurrence of business cycle at regular intervals of time. However, periods of intervals are different for different business cycle. There is a general consensus that a normal business cycle can take 7 to 10 years to complete.

General nature

The general nature of a business cycle states that any change in an organisation affects all other organisations too in the industry. Thus, general nature regards the business world as a single economic unit.

For example, depression moves from one organisation to the other and spread throughout the industry. The general nature is also known as synchronism.

Types of Business Cycle

Following the writings of Prof .James Arthur and Schumpeter, we can classify business cycle into three types based on the underlying time period of existence of the cycle as follows:

1. **Short Kitchin Cycle**
2. **Longer Juglar cycle**
3. **Very long Kondratieff Wave**

Short Kitchin Cycle (very short or minor period of the cycle, approximately 40 months duration)

Longer Juglar cycle (major cycles, composed of three minor cycles and of the duration of 10 years or so)

Very long Kondratieff Wave (very long waves of cycle, made up of six major cycles and takes more than 60 years to run its course of duration)